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TAGS: [EFIN](#) [EINV](#) [ECON](#) [RS](#)

SUBJECT: RUSSIA: PRICEWATERHOUSECOOPERS WITHDRAWS AUDITS OF  
YUKOS

REF: A. MOSCOW 1997

[1](#)B. MOSCOW 466

Classified By: Acting ECON M/C Laura Lochman, Reasons 1.4 (b/d).

[1](#)1. (C) Summary: PricewaterhouseCoopers Russia (PwC) Managing Partner Peter Gerendasi confirmed press reports from the week of June 25 that the auditing firm had withdrawn its 1995-2004 audits for former oil giant Yukos. Gerendasi volunteered few details about the circumstances under which PwC's senior management became aware of the information about Yukos that prompted the decision to withdraw. He mentioned only that "investigators" presented documents reflecting Yukos internal structures and contractual relationships that had not been available for PwC to assess and investigate during the course of its audits for Yukos. Gerendasi explained that PwC made its decision to withdraw in consultation with company headquarters in the U.S., and only after a thorough internal review that compared its audit records with the recently-presented information.

[1](#)2. (C) Turning to other issues affecting PwC, Gerendasi said that the Federal Tax Service (FTS) had filed a request for the Finance Ministry to conduct a review of PwC's audit practices (Ref A). The review, which is set to begin July 9, will assemble government officials as well as subject matter experts to evaluate PwC's policies, organizational structures, and methodology. On July 10, proceedings begin for PwC's appeal of the March 20 Federal Arbitration Court (FAC) decision that from 2002-2004 Yukos and PwC colluded to defraud the GOR. On July 17, the Supreme Arbitration Court will begin hearing PwC's appeal of the FAC decision which found that in 2002 PwC had improperly accounted for expatriate salaries and, consequently, owed the Russian government USD 14 million. As a result of the latter FAC decision, the Ministry of Interior began a criminal investigation in early February that has not led to any charges to date (Ref B). End Summary.

Withdrawal of 1995-2004 Yukos Audits  
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[1](#)3. (C) PricewaterhouseCoopers Russia (PwC) Managing Partner Peter Gerendasi told Econoff July 3 that press reports from the week of June 25 regarding PwC's decision to withdraw its 1995-2004 audits of former oil giant Yukos were accurate. He said that PwC had become aware of information about Yukos that the former oil giant's management had not made available during the course of the audits. (Note: He did not specify

when PwC became aware of this information. End Note.) He mentioned only that "investigators" had presented documents that outlined Yukos operational and administrative structures, contractual relationships with suppliers and distributors, and various holdings which Yukos management had not made available to PwC auditors. (Note: It is possible that the Prosecutor General's office obtained this information in the course of the tax evasion and money laundering investigations against Mikhail Khodorkovsky and Platon Lebedev. Under such a scenario, the Prosecutor General's office may have made a determination that PwC was a victim of Khodorkovsky's fraud, which means that disclosing such information obtained in the course of a criminal investigation would not have been improper. End Note.) Gerendasi commented that any auditing firm would have investigated information of this nature to determine the accuracy of any and all associated transactions as well as to assess the relationship between the firm being audited and its business partners. He explained that the "new" information was carefully reviewed and ultimately deemed credible. He said that the senior management of PricewaterhouseCoopers Russia-CIS consulted closely with the company's U.S. headquarters and concluded that, since Yukos was no longer a going concern, the only viable option was to withdraw its audits. On June 15, PricewaterhouseCoopers Russia-CIS General Director Mike Kubena informed Yukos board chairman Viktor Gerashchenko and Yukos receivership manager Eduard Rebgun that PwC had withdrawn its audits of Yukos in accordance with international auditing standards and Russian law. On June 22, PwC issued a public statement to this effect.

#### Finance Ministry Audit Review

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14. (C) In April, the Federal Tax Service (FTS) filed a request that the Finance Ministry initiate a review of PwC's auditing practices (Ref A). PwC provided the Finance Ministry a comprehensive report that describes the organizational structure as well as management policies and auditing standards and practices. The review is scheduled to begin the week of July 9. The FTS request stemmed from recent court decisions against PwC. Specifically, in November 2006, PwC lost its second appeal of a Federal Arbitration Court decision that the auditor had improperly accounted for expatriate salary expenses in 2002 and, consequently, owed USD 14 million in back taxes. As a result of the FAC decision, the Ministry of Interior (MVD) launched a criminal investigation, which included confiscating PwC documents in a raid on March 9. Moreover, FTS began another investigation of PwC's expatriate salary accounting practices, this time looking at the period 2003-2005. The other court case underlying the FTS request was the FAC decision on March 20 that underlying contracts for PwC's 2002-2004 audits of Yukos were invalid because they were premised on an unlawful purpose. The FAC supported the tax authorities' argument that PwC colluded with Yukos to defraud the government and had, therefore, falsified its audits.

#### Pending Appeals

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15. (C) Gerendasi said that on July 10 the Supreme Arbitration Court would begin hearings of PwC's appeal regarding the 2002 expatriate salary case. He expressed "quiet optimism" that PwC would prevail since "the referring judge deemed our case to have merit." Nevertheless, he observed that the MVD had not yet closed its related criminal investigation. He noted that MVD officials had interviewed approximately 50 members of PwC's staff and would interview another 150 before the criminal investigation ended. According to Gerendasi, unless the authorities uncover credible evidence of criminal intent by mid-August, they would be forced to close the investigation, which began February 1.

16. (C) Gerendasi also noted that the appeal of the March 20

FAC decision regarding the 2002-2004 Yukos audits would begin on July 17. He said that PwC's legal counsel was uncertain what effect PwC's decision to withdraw its Yukos audits would have on the outcome.

Comment

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17. (C) Gerendasi appeared unwilling, and in any case may have been legally unable, to discuss details on the source and circumstances under which PwC became aware of this new information about Yukos. He was also unequivocal that the withdrawal, although he characterized it as PwC's only viable option, was nonetheless a difficult call. He suggested that the withdrawal would not have an adverse effect on the Finance Ministry's review of PwC's auditing practices. We maintain our outlook that the relative lack of progress in the MVD's criminal investigation is a good sign that no one from PwC will be facing criminal charges any time soon. End Comment.  
BURNS